

# **A COMMUNITY BASED LAND TRUST (CBLT) MODEL FOR SASKATCHEWAN AGRICULTURE<sup>1</sup>**

by

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## **Introduction**

Saskatchewan agriculture faces many serious problems that involve the ownership and transfer of agricultural land. These include the difficulties of intergenerational transfer, security of land tenure, excessive farm debt and the longer term environmental issues of preservation of wildlife habitat and suitable land stewardship practices. In the past, groups of Saskatchewan people organized, often in the form of cooperatives, to address the problems facing the community. Perhaps part of the solution to the problems relating to agricultural land can also be solved by cooperative action from within the community.

## **The Community Based Land Trust (CBLT) Concept**

A CBLT is a democratic organization that holds land for the benefit of the community. There are over 600 CBLTs in North America with many forms of organization, ownership and control mechanisms.

The initial CBLT concept grew out of the recognition that the control of the land base by the community was required if the aspirations of the community were to be met. Each CBLT is different because of the need to address these local aspirations and local conditions.

A CBLT may obtain land either through purchase, by donation or transfer in lieu of shares. The title to the land is usually held in perpetuity so that it is removed from the speculative market. Appropriate uses for the land are determined in a process comparable to public planning or zoning and the land is then leased. Normally, the leases are lifetime or long-term leases, which may be transferred to the leaseholders' heirs if they wish to continue to use the land. The fee charged to the leaseholder may be a regular lease fee, based on "productive value" rather than "full market value" of the land.

## **Objectives**

The specific objectives of the CBLT model are:

- 1) to serve as an option to those farmers facing the problem of intergenerational land transfer when the next generation has to borrow money to buy assets (land) in order for the previous generation to retire in some comfort and dignity.

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- 2) to serve as an option to those farmers wishing to acquire long term secure leases on farmland as an alternative to ownership.
- 3) to serve as an option to those farmers facing foreclosure or debt restructuring.
- 4) To serve as an option for those individuals or organizations wishing to purchase an investment vehicle that reflects agriculturally related returns, is financially liquid, has low administration fees, and is backed by real agricultural assets

### **Capital Acquisition**

The CBLT will acquire its capital through the transfer of land, therefore no land will be purchased or money borrowed. On transferring the land the transferrer will be issued a Class A unit and a number of representative acre units (RAUs).<sup>3</sup> The transferrers of land (capital providers) can be farmers facing financial difficulty; farmers who need money to retire and also wish to pass the farm onto their children; and financial institutions, both private and government, who currently own land through foreclosure. The transferrers of the land will have the exclusive right to designate whom the tenants will be as long as the person is a community resident and will be actively farming within the community. If a capital provider is a corporation or government agency it will receive one Class A unit which will be held in trust by a representative that is also a community resident (not necessarily a company or agency employee) and who is given the authority to exercise the voting privilege.

Tenants would have the right at any time to purchase the rented land from the CBLT. To do so, the tenant will purchase RAUs equivalent to the number of RAUs designated to the land he/she is currently renting and wishes to own, these RAUs will then be turned over to the CBLT in exchange for the land title. Upon completion of the land transfer, these RAUs, and the tenants Class A voting unit would be removed from the CBLT. Given the secure tenure provided in the lease and the economies of size in farming, it is anticipated that the vast majority of tenants will prefer to purchase land outside the CBLT, and therefore, will not exercise this option.

### **The Calculation of RAUs for a Parcel of Land**

It is important that the number of RAUs for a particular piece of land be calculated fairly in relation to all the land in the CBLT. The calculation must account for varying land quality; be consistent throughout the CBLT; and account for as much of the variation in the market value of land as possible. Each RAU in a CBLT must be of the same value to the holder and generate the same income in a given year.

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<sup>3</sup> In financial security markets these representative acre units (RAUs) would be known as Class B nonvoting shares.

The number of RAUs issued for a parcel of land is based on the Saskatchewan Crop Insurance Corporation's (SCIC) rating of the land in question with respect to its long term (15 year moving average) wheat on summer fallow yield. One RAU per cultivated acre will be issued for land that has a 30 bushel wheat on summer fallow yield, with the number of RAUs per cultivated acre being adjusted according to the long term yield. Pasture land is compared to cultivated acres by a 5:1 ratio. Wasteland has zero value in the calculation of RAUs.

### **Lease Terms**

The terms of the lease deal with tenant eligibility, tenure length, amount and type of annual payments and rules for termination. The eligibility of the tenant is restricted to community residents. The length of the lease is for the life of the lessee with the right to transfer it to next-of-kin or other beneficiary during life or at death as long as the transferee is or will become within a reasonable length of time (1 to 2 years) a community resident. All tenants will be required to designate an heir as part of the terms of the lease, failure to comply will result in no lease being granted. Subleasing will only be approved on a yearly basis and for reasons deemed important by the board such as health, compassion, and short term employment contracts outside the community.

The lease can be terminated by the lessee without penalty at any time between the months of November and February of each year. If the lease is terminated in the other months the former lessee is responsible for the costs incurred by the CBLT to have the land farmed in the meantime. When new tenants, designated by the former tenant, refuse to take over the lease the CBLT will choose a tenant by a majority vote of the board of directors based on the selection rules outlined in the bylaws of the CBLT. The CBLT can terminate the lease for nonpayment at due dates; unauthorized subletting of the land, and poor farming practices as determined by previously agreed upon levels of weed infestation, soil erosion, or other land stewardship issues. The tenant will be held responsible to pay for any corrections required due to poor farming practices.

The timing of the lease payment is important as it affects the cash flow of the tenant and the return to the RAU holder. Therefore, 1/2 the payment is made by February 1, in the year the crop is to be grown, with the payment based on last year's CWB price for #1 HRSW or the GRIP price, whichever is greater, the remainder of the lease payment is due November 1.

### **Calculation of the Lease Payment**

The lease payment per RAU will be the cash equivalent of 5 bushels of #1HRSW, basis in store Thunder Bay less elevation, transportation and dockage costs or the GRIP price, whichever is greater. The 5 bushels represent 1/3 of a wheat and summer fallow rotation yielding 30 bushels per acre of wheat one year and 0 in the summer fallow year.

### Buildings and Other Improvements

The CBLT will take ownership of all buildings and improvements on land transferred to it but will not include their value in the calculation of RAUs and, will not pay the transferrer for them nor charge the tenant additional rent. As a result farmers who wish to be compensated for buildings and improvements will most likely choose not to transfer the land in question to the CBLT. Others who wish to designate children or grandchildren as lessees in the CBLT may still offer the land to the CBLT even though the land has substantial buildings or improvements. The new tenants can use the buildings rent free but will be responsible for the safe use and operation of the buildings. The tenant may wish to take out insurance to protect against liability for accidents arising out of the legitimate use of the buildings. Safety considerations will dictate that derelict buildings be torn down before the CBLT will accept the land. Therefore, it is up to the transferrer to decide what land is to be transferred to the CBLT. However, home quarters will not be transferable to the CBLT due to possible conflict with other legislation.

Compensation by third parties for the use of land e.g., oil wells, will be paid directly to the tenant from the oil company as payment is for the inconvenience of having to adjust farming practices. Land with such oil wells and other easements will be accepted by the CBLT but the transferrer will not be compensated for them.

Finally, the tenant may wish to improve the land farmed by either clearing and/or breaking parts of it or erecting buildings. The CBLT board would have to approve any such action as it must be deemed to be consistent with land stewardship and conservation. The tenant has the choice of whether or not to receive more RAUs for the new land in the case of clearing and breaking. If the tenant decides to receive more RAUs for the new land, he/she could sell them to cover the clearing and breaking costs but will also have to pay rent on the new RAUs. If no new RAUs are taken the rent will stay the same. Similarly, if land is improved e.g., by the planting of shelter belts, this must have the approval of the CBLT board but will not change the RAU designation. Finally, the erection of new buildings must be approved by the CBLT board beforehand and all new buildings will become the property of the CBLT but will not change the RAU designation. Therefore, it is up to the tenant to study the economic implications of buildings and improvements before they ask the CBLT board for approval.

### **Return to RAU Holder**

The total financial return to the RAU holder includes both the annual lease payment and capital gain/loss after income tax. The RAU holder will receive the annual lease payment less property taxes and CBLT administration fees as a cash payment once per year in May. This date needs to be consistent from year to year as the RAU value may adjust slightly as the payment day approaches. In addition the RAU holder can sell the RAU at any time to another individual or institution and realize a capital gain or loss based on the sale price less the purchase price.

The calculation of property tax per RAU will be done by taking the total assessed value of the land owned by the CBLT and multiplying it by the mill rate. The resulting values will then be added together and divided by the number of RAUs in the CBLT.

The CBLT administration fees will be based on the actual costs of running the CBLT but should be restricted to a maximum of 5% of total rental income collected. These administration fees will include the cost of transferring the land into the CBLT, (the average will be approximately \$500 per quarter section, but can range from \$200 to \$2,000). Therefore land transfers to the CBLT should be handled on a once a year basis where a discount could be negotiated for volume.

An historical analysis was done to determine the RAU value. The method uses the capitalization formula to calculate the value of the RAU from one year to the next. The capitalization formula divides the net rental income per RAU by the appropriate interest rate for that year. The interest rate used in the historical analysis was that for government bonds of greater than 10 years. The interest rate used in the future by the "market" will depend on its perception of the relationship between RAU returns and those of the rest of the market. The RAU returns were found to be somewhat counter cyclical to the rest of the market. If the inclusion of RAUs reduce the risk of a well diversified portfolio the interest rate will be low and very close to the "risk free" rate. The rate associated with 90 day government T-Bills is commonly referred to as the risk free rate. The lower the rate that the market uses to discount future RAU incomes the higher their value. For example, if an RAU was trading in 1992, its lease payment would be approximately 5 bushels x \$3.50/bushel = \$17.50. The rental income per RAU for the holder if property tax and CBLT administration fees are \$5 would be \$12.50. If the market perceives that the RAU returns will move with other investment vehicles, thereby not contributing to diversification it's value may be  $\$12.50/10\% = \$125/\text{RAU}$ . However, if the market perceives that the RAU return will move counter cyclical with other investment vehicles and thereby contribute to diversification the value may be  $\$12.50/5\% = \$250/\text{RAU}$ . Currently average Saskatchewan farm land is selling for \$236/acre.

### **Ownership and Control of CBLTs**

The ownership of the CBLT should be open to as large a capital pool as possible but be controlled democratically by a combination of RAU holders and tenants most of whom are community residents. In addition, some individuals may buy RAUs through their self-directed RRSP, thereby securing access to the returns associated with farmland with before tax dollars rather than with after tax dollars as is the case when acquiring clear title.

The CBLT will be controlled by a board of directors consisting of 1/3 nonresident RAU holders who hold a minimum 160 RAUs, 1/3 community resident RAU holders who hold a minimum 160 RAUs, and 1/3 tenants. Therefore, 1 Class A unit will be issued to all tenants and investors holding a minimum of 160 RAUs

whether or not they are community residents. If at any time the total non-residents RAU holdings are below 1/3 of the total RAUs outstanding, then their representation will decrease accordingly. The same is true for resident RAU holders. Therefore, if in the early stages of the CBLT no RAUs are held outside the community, the board will consist of 50% resident RAU holders and 50% tenants. Likewise, if the RAUs are held entirely outside the community, the board will consist of 50% non-resident RAU holders and 50% tenants.

### CBLT Board Powers

The CBLT board will be responsible for enforcing the terms of the lease agreement, that is, collecting lease payments; ensuring proper farming practices are followed; cancelling leases if tenants renege on their obligations; approving new buildings and improvements; and selecting and approving new tenants when the need arises. The CBLT board would **not** have the power to adjust the lease payment or its due dates.

The CBLT board will automatically approve a new tenant if he/she is the next-of-kin of the former tenant and a community resident. If the new tenant is **not** the next-of-kin of the former tenant or the former tenant gives up the lease due to noncompliance with its terms, the CBLT board will choose a new tenant. Financial institutions which transfer land to the CBLT will give the current tenant and former owner first and second right of refusal respectively to become the CBLT tenant. If either of these is not eligible the responsibility for choosing a new tenant passes to the board of directors of the CBLT.

### **Dissolution of the CBLT**

The dissolution procedures of the CBLT should be set up in the articles of incorporation. In the event the board of directors votes to dissolve the CBLT, a vote must also be held by the RAU holders. The RAU holders will have a vote for each RAU owned and a 2/3 majority for dissolution must occur for the CBLT to dissolve. In the event of dissolution the assets (land) should be sold at fair market value with the first right of refusal to the tenants or their next-of-kin. Proceeds of the sales will be paid to the RAU holders.

### **Conclusion**

The CBLT concept has the potential to address some of the major problems currently facing the agricultural industry in Saskatchewan. The CBLT model can serve as an option to those farmers who cannot meet their goals under the present land tenure system. It can also serve as an option to those investors who wish to acquire assets that have some of the return characteristics of agricultural land. The CBLT model is relatively new and may require further refinement and a pilot project to determine its feasibility. However, as one participant of the farmer focus group said; "if it is going to work anywhere, it will probably work in Saskatchewan because of the cooperative nature of the people."